Before the

Federal Trade Commission

Washington, D.C.

United States Postal Service Study

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National Association of Letter Carriers Comments on Competitive Advantages and Disadvantages of the United States Postal Service Regarding Competitive Products

The National Association of Letter Carriers, AFL-CIO, (NALC), respectfully submits its comments to the Federal Trade Commission (FTC) regarding the study of United States Postal Service (USPS) competitive advantages and disadvantages over private delivery services with regards to competitive products, which was initiated by the Postal Accountability and Enhancement Act (PAEA), PL 109-435. NALC is a national labor organization which represents, for purposes of collective bargaining, the approximately 225,000 city letter carriers employed by the USPS nationwide.

Overview

There is no basis whatsoever for any allegation that the USPS is using its monopoly on letter mail or any other alleged advantage to dominate competitive areas. Over the past 35 years, the USPS has been subject to substantial legal and regulatory restrictions which have impeded its ability to compete against private sector companies offering competitive products and services. These restrictions include:

1. Limited pricing flexibility,
2. Inability to respond to pricing needs in a timely manner,
3. Maintaining a Universal Service Obligation and Uniform Pricing,
4. Restrictions on ability to negotiate agreements with large mailers,
5. Restriction on typical business decisions, and
6. Competitors' use of USPS' public status for advantages.

Each of these factors will be discussed in greater detail below.

First, as it has done in recent decades when enforcing the nation's antitrust laws, the FTC should apply a market test in its analysis of the relative position of the Postal Service and its competitors. Such a test shows that the Postal Service's market share in competitive markets has consistently declined. In 1971, the USPS delivered 50 percent of the nation's parcels; today its share is less than 5 percent. In 1978, the USPS had 100 percent of the express mail market; today it has just 7 percent of the market. Over time, the Postal Service's commanding position in the

Priority Mail (two-day delivery) has been cut in half. These market tests clearly demonstrate that any allegation that the USPS is competing unfairly should be rejected out of hand.

Second, any supposed advantages the Postal Service might have at the micro level (property taxes, exemptions from parking tickets, etc.) are far outweighed by the burdens placed on it at the macro level by the law. Most notably, the USPS has a Universal Service Obligation and virtually every aspect of its operations is constrained by public policies set by Congress. These range from hiring preferences for veterans to pricing rules that raise the cost of international air transport for the Postal Service. No private company must satisfy a regulatory agency created specifically to scrutinize every pricing and service decision it makes; nor do they face the level of Congressional oversight that comes with special committees with jurisdiction over all postal matters.

Third, any analysis of the Postal Service's market position today may be of historical interest, but going forward, the passage of the Postal Accountability and Accountability Act of 2006 will significantly affect the competitive position of the Postal Service relative to its private competitors. Although the new law applies the nation's antitrust laws to the Postal Service for the first time, the regulations for competitive product pricing have not yet been issued. Congress debated whether to directly specify these rules and regulations for competitive services in the law. It rejected calls by the major private companies to mandate "stand-alone" pricing, just as it rejected earlier proposals to require the Postal Service to set up a "private law company" through which to deliver competitive services. Rather, Congress endorsed the traditional approach to pricing (based on incremental costs), but decided to leave the details of competitive product pricing to the new Postal Regulatory Commission. It is too early to know how the PRC's rules will affect the relative positions of the Postal Service and its private competitors. But the new law is unlikely to alter the basic market landscape facing the Postal Service. The new law forbids the USPS from engaging in joint ventures or investing in allied "non-postal" services (logistics, etc.) that have been used by the private companies to expand their market shares. Given the uncertainty facing the Postal Service in the area of competitive services, any conclusion the FTC comes to in this exercise will be premature at best. Indeed, the more important analysis of the Postal Service's activities in the competitive services area will come in five years. Under the new law, the Postal Regulatory Commission is to conduct a review of the rules governing the Postal Service's participation in competitive markets.

The Postal Service and Competitive Services

As it considers the alleged advantages enjoyed by the Postal Service as it relates to competitive services, the FTC should consider the regulatory restrictions and limitations that have faced the Postal Service over the years. Most of these restrictions will remain in place under the new law.

Limited Pricing Flexibility. As the parcel market is dominated by large volume business senders, pricing is of the utmost importance in gaining market share. Yet, even though the USPS must run its business under a regulator (the Postal Regulatory Commission or PRC), its pricing mechanism is now very restrictive. Prices are not set according to goals such as generating business, gaining market share, or the successful launching of new products, but based largely on a cost-allocation scheme the regulator (PRC) adopts. This arrangement allows the Postal Service's private competitors, whose pricing decisions can be made quickly and freely, to undercut the pricing of USPS products and services by just a small amount.

In addition, the USPS undergoes a lengthy process to assure that each competitive product is priced in a manner to cover all the costs that it incurs in that particular product. However, there is no restriction on its competitors, who can subsidize any products with more profitable products in order to grow market share and become the dominant provider in that area.

Inability to Respond to Pricing Needs in a Timely Manner. Because the USPS is required to file rate cases, which require a time frame for public comments and regulator review, it cannot change its prices quickly to respond to market conditions. If a private competitor wishes to undercut the USPS pricing on specific products, not only will that competitor be able to move prices more often and in a less restrictive manner, but it will also be able to know what the USPS price will be far in advance of the implementation. This advantage allows competitors to attract virtually all price sensitive senders of competitive products.

Universal Service Obligation and Uniform Pricing. The cost of offering a Universal Service Obligation (USO) is also a factor which raises the cost of the USPS business model. The USPS must service more than 140 million delivery points each day, six days a week, no matter how costly and it must charge all of its customers essentially the same prices. This is in the national interest as it has helped create national markets and has permitted all Americans to participate in the nation's economic, cultural and social activities. However, since it cannot discontinue serving non-profitable areas or use pricing decisions to direct costly customers to its competitors, the Postal Service is disadvantaged when pricing competitive services in profitable market segments, be they commercial or geographical in nature. The cost of the USO has been estimated and debated by many parties in the past. But, in a multi-billion dollar market, there is no debate that the resulting cost disadvantage has shifted competitive markets decisively in favor of the private companies.

Of course, the USO is also an asset to the private competitors which, at times, rely on the USPS to provide the last mile of their service in expensive delivery areas. Taking advantage of the limited pricing flexibility it has available to it, the USPS introduced drop-ship discounts over the past decade with the Parcel Select option. This allows companies to pass off the parcels that are more costly to deliver on to the Postal Service for final delivery. The biggest customers of Parcel Select have been the private competitors: UPS, FedEx and DHL together account for 67 percent of Parcel Select volume.

Although Uniform Pricing is positive for Americans and their businesses located in costly-to-serve communities in both urban and rural areas of the country, it has been a major disadvantage to the USPS for competitive products. Uniform Pricing requires the USPS to offer the same price on a product, no matter where it is being sent to or from. Such a pricing scheme naturally attracts the most expensive deliveries, as USPS pricing is undercut by private competitors on virtually all high-margin deliveries. Through flexible pricing, private companies can essentially choose what deliveries to make by adjusting prices using a zip code-to-zip code system. Price sensitive mailers (specifically businesses, who account for approximately 87 percent of the parcels sent) will naturally flock to the private companies for high-margin deliveries (where the USPS pricing is undercut), but go with the USPS for costly deliveries – as private operators can add surcharges to avoid taking on these costly deliveries. (This process has long been referred to as cream-skimming in academic studies.)

As the size of the private competitors' networks grew over time, their share of the parcel market grew as they were able to undercut USPS prices in the most lucrative markets. Thus, the USPS share has declined over time.

Restrictive Process for Agreements with Mailers. The USPS, which is more than two centuries old, has negotiated only five agreements (Negotiated Service Agreements) with mailers, which provide discounts based in part on volumes. Only three such agreements have, as of today, made it through the regulatory process and gained approval (one is pending, the other was withdrawn.) None of the five were in the area of competitive products. In addition, the USPS is forbidden from negotiating agreements that exclude the use of competitors, such as UPS, FedEx, or DHL.

Of course, private companies are free to enter into such service agreements, including agreements which exclude competitors such as the USPS.

Restrictions on Typical Business Decisions. Unlike private competitors, USPS has serious restraints on how it manages its financial resources. For example, USPS is limited to investing its funds in government treasury bonds. In addition, the USPS cannot take part in acquisitions or mergers. Often private sector companies merge or buy competitors in order to strengthen its business in certain areas. The USPS is required to build infrastructure from the ground up in virtually every circumstance, and maintain it.

The USPS also has very limited ability to introduce new products and services. First it has to convince the regulator that any such new product or service is appropriate and feasible. Competitors can actively participate in arguing against allowing the USPS to do so. No private competitor is subjected to such restrictions.

Competitors Use of Public Status for Advantage. Competitors have another unique advantage over the Postal Service: they can lobby and utilize the status of the USPS for competitive advantage. USPS' competitors were actively involved in crafting the PAEA. In fact, the origin of this very FTC study traces back to USPS private sector competitors' lobbying efforts.

In addition, competitors can influence postal policy by providing comments and/or presenting evidence to agencies with jurisdiction over the Postal Service. This is, quite obviously, a one-way street. The USPS and the affiliated employee organizations cannot lobby against or use public hearings to affect the private delivery companies' operational plans, pricing, new products or related matters. In fact, the USPS is not allowed to lobby at all.

Conclusion

The USPS, a delivery service with a public service obligation, is burdened with many regulatory disadvantages; these disadvantages will not disappear under the new law. The fact that USPS' share of competitive markets has steadily declined over time confirms that these disadvantages outweigh whatever advantages other interested parties may cite.

This basic conclusion raises serious questions about the essential utility of the FTC's study. A more useful study would focus less on the relative advantages and disadvantages of the Postal Service and more on traditional matters of consumer welfare and anti-trust concerns. There was a time when the FTC focused its attention on the negative economic impact of concentration in product and service markets. Such scrutiny is needed today more than ever. Given this, it is ironic that the FTC has been tasked to closely examine the activities of a relatively minor player in competitive postal markets – the USPS – instead of those of private companies that have amassed huge market shares in the ground parcel and express delivery segments of the market. The FTC should examine this more important aspect of competitive postal markets in the near future.